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SUBJECT: KAZAKHSTAN: SOCAR DISCUSSES TRANS-CASPIAN OIL
TRANSPORTATION SYSTEM

REF: (A) ASTANA 2266 (B) ASTANA 2317

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11. (U) Sensitive but unclassified. Not for public Internet.

12. (SBU) SUMMARY: On December 12, Energy Officer met with Vurgun Jafarov, State Oil Company of the Azerbaijan Republic (SOCAR) Country Director for Kazakhstan, and Fuad Khodjayev, SOCAR Country Manager, to discuss the November 14 agreement between SOCAR and KazMunaiGas (KMG) to develop a trans-Caspian oil transportation system. The proposed system would ship crude from Eskene (near Atyrau on Kazakhstan's northwestern Caspian coast) to Baku via pipeline and tanker. Jafarov said SOCAR and KMG will establish a 50-50 joint venture and are capable of carrying out the project independently, although he acknowledged that certain details -- such as who will build and upgrade port infrastructure in Kazakhstan, who will build and own the tankers, and what transit tariffs the joint venture will charge -- have yet to be negotiated. Also on December 12, SOCAR and KMG officials delivered a presentation in Baku to the regional vice presidents of international oil companies with major upstream assets in Kazakhstan and stressed to them that the project will need guaranteed delivery of oil from Tengiz, Karachaganak, and Kashagan in order to move forward. END SUMMARY.

13. (SBU) Aspects of the November 14 agreement have been reported previously (reftel A), but this was the first opportunity to discuss specifics with SOCAR representatives in Kazakhstan, who arrived in September and are still renovating their new office. The proposed trans-Caspian oil transportation system would ship Kazakhstani crude westward via pipeline from Eskene to Kuryk, then via tanker from Kuryk to Baku, and from there to global markets via the Baku-Tbilisi-Ceyhan (BTC) pipeline, Baku-Supsa pipeline, or trans-Caucasus railway to Batumi or Kulevi on Georgia's Black Sea coast.

SOCAR DOES NOT NEED INTERNATIONAL PARTNERS

14. (SBU) Jafarov confidently claimed that SOCAR and KMG could complete this three-year, \$3.5 billion project without outside

assistance. Specifically, he asserted that KazTransOil, a wholly-owned subsidiary of KMG, has the expertise and capital required to build the 840-kilometer Eskene-Kuryk pipeline without an international partner and that KazMorTransFlot can independently handle the necessary upgrades to port infrastructure and facilities at Kuryk. The 50-50 joint venture between SOCAR and KMG "does not need other partners," he said and added jokingly, "we will divide the Sea between us." (NOTE: Arman Darbayev, Executive Director for Oil Transportation at KMG, told Energy Officer that KMG would prefer to invite international companies to take an equity stake in the project, but SOCAR has resisted this and KMG is reluctant to reduce its share below that of SOCAR. Furthermore, KazMorTransFlot officials told Embassy Political Officer on November 6 (reftel B) that they have had difficulty recruiting qualified personnel and acquiring tankers of sufficient size to meet demand. END NOTE).

CRUDE SHIPMENT COMMITMENTS KEY TO PROJECT SUCCESS

15. (SBU) Jafarov confirmed media reports that SOCAR and KMG plan to launch the project in 2009 and complete activities by 2012. He did not say whether or not feasibility studies -- for example, to deepen the port at Kuryk or construct single-point mooring buoys -- had been commissioned or conducted. Although he claims SOCAR and KMG can manage the infrastructure investments independently, Jafarov emphasized that international companies with major upstream assets in Kazakhstan must commit to shipping their crude through the system if the project is to move forward. Consequently, on December 12 in Baku, senior officials from SOCAR and KMG presented their business case to regional vice presidents from companies invested in Tengiz, Kashagan, and Karachaganak.

TANKER FLEET QUESTIONS REMAIN

16. (SBU) Jafarov insisted that "there are no outstanding issues that could delay the start of the project," but he acknowledged that

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agreement has not been reached on the size, location, or ownership of the proposed trans-Caspian tanker fleet. For logistical reasons, according to Jafarov, the tankers would have to be built in the Caspian Sea, most likely the Russian port of Astrakhan. The preference would be to build 60,000 deadweight-ton (dwt) double-hull tankers, but if there are delays or disputes that prevent construction of these vessels, Jafarov said the project could still work, using existing Azeri and Kazakhstani tankers already in the Caspian. He noted, for example, that Azerbaijan and Kazakhstan each own five 13,000 dwt tankers and several smaller vessels that already transport oil from Aktau to Baku, including shipments of up to 100,000 barrels per day from Tengizchevroil. In a sense, he asserted, the trans-Caspian oil transportation project is already up and running.

BAKU-SUPSA PIPELINE A CONVENIENT BACK-UP

17. (SBU) When asked whether the Baku-Supsa pipeline would be available to Kazakhstani exporters, Jafarov said the pipeline is operated by the Azerbaijan International Operating Company (AIOC) and access rights would have to be negotiated with AIOC, not SOCAR or the Government of Azerbaijan. He called Baku-Supsa a "convenient little pipeline" that was recently modernized and said it has been a useful backup to the much larger BTC transport route. Jafarov also expressed some concern that large volumes of Tengiz crude, which is high in sulfur, would adversely affect the quality of Azeri crude in either the Baku-Supsa or BTC pipelines. (NOTE: The capacity of the pipeline is 145,000 bpd. After an explosion and fire closed BTC on August 6, the Baku-Supsa pipeline was used to re-route Azeri oil deliveries. END NOTE).

18. (SBU) COMMENT: Although the November 14 agreement between KMG and SOCAR represents real progress toward the development of a trans-Caspian oil transportation system, it is still unclear who will do what, and when, to make that system a reality. For example, both Chevron and ExxonMobil have said they will take the lead on building the pipeline from Eskene to Kuryk, which is the first component of the proposed system, but no final decision has been made and a new consortium will likely be established to conduct a

feasibility study and build this segment. In addition, reftel B raises questions about KazMorTransFlot's expertise and capacity to upgrade the port and terminal facilities on its own, while international oil companies remain very concerned about unresolved maritime safety and tanker transportation issues. Clearly, KMG would prefer to invite external partners to contribute their financial and technical assistance, while SOCAR insists the two national oil companies do not need outside help. These questions are complicated and serious and suggest that the negotiations between KMG and SOCAR are just beginning. END COMMENT.

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